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CITATIONS

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In the Supreme Court of the United States

OCTOBER TERM, 1947

No. 462

TRANSAMERICA CORPORATION AND ITS OFFICERS AND DIRECTORS, PETITIONERS

v.

SECURITIES AND EXCHANGE COMMISSION

No. 463

TRANSAMERICA CORPORATION AND ITS OFFICERS AND DIRECTORS, PETITIONERS

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinions of the District Court (R. 62a–75a, 79a–80a) are reported in 67 F. Supp. 326, and the opinion of the Circuit Court of Appeals (R. 116–27) is reported in 163 F. 2d 511.

JURISDICTION

The judgments of the Circuit Court of Appeals with respect to which the writs of certiorari are sought were rendered on September 15, 1947 (R. 128–29). Petitioners invoke the jurisdiction of

this Court under Section 240 (a) of the Judicial Code, 26 Stat. 828, as amended, 28 U. S. C. 347 (a), which is made applicable by Section 27 of the Securities Exchange Act of 1934, 48 Stat. 902, 15 U. S. C. 78aa.

QUESTIONS PRESENTED

1. Whether the Commission's Rule X–14A–7, promulgated under the Securities Exchange Act of 1934, is invalid to the extent that it imposes as a condition to proxy solicitation by a corporate management the requirement that the management permit stockholders to vote, by means of the proxy, upon proposals submitted by an independent stockholder in accordance with the provisions of the Rule.

2. Whether, under Delaware law, the stockholders of a Delaware corporation may properly act upon a resolution that an account of the proceedings at the annual meeting be sent to all the stockholders of the corporation.

3. Whether the judgment of the District Court, as affirmed by the Circuit Court of Appeals, is invalid on the following grounds: (a) because it is too broad; (b) because it does not take account of changed circumstances; (c) because it directs the inclusion of a stockholder's proposals in the notice of meeting notwithstanding the fact that the Commission's proxy rules do not expressly deal with the contents of a notice of meeting; (d) because it directs the sending of a notice of meeting to persons not solicited for their proxies;

and (e) because it is concerned with the enforcement of an alleged State-created right.

STATUTE AND RULES INVOLVED

The statutory provision involved is Section 14 (a) of the Securities Exchange Act of 1934, 48 Stat. 895, 15 U. S. C. 78n (a) ("The Act"), which confers upon the Securities and Exchange Commission ("the Commission") authority to make rules and regulations governing solicitation of proxies in respect of any security registered on a national securities exchange. The rule most particularly involved is Rule X–14A–7, dealing with proposals of independent security holders. The provisions of Section 14 (a) and of Rule X–14A–7 are set forth, and the proxy rules are described generally, at pp. 3–5, *infra*.

STATEMENT

The instant proceeding began as an injunction action instituted by the Commission to enforce compliance with rules it has promulgated under Section 14 (a) of the Securities Exchange Act of 1934. That section provides as follows:

> It shall be unlawful for any person, by the use of the mails or by any means or instrumentality of interstate commerce or of any facility of any national securities exchange or otherwise to solicit or to permit the use of his name to solicit any proxy or consent or authorization in respect of any security (other than an exempted se-

> curity) registered on any national securities exchange in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

The rules prescribed by the Commission under this Section are entitled "Regulation X–14" and are printed in their entirety at R. 88–112. The rules are designed not only to ensure that security holders shall be fully informed concerning matters that will arise at the annual meeting but also to ensure that their voting rights shall be effective. Proxies may not be solicited unless the security holders are furnished with a proxy statement which shall have been submitted to the Commission at least ten days prior to mailing.[1] The proxy statement must contain information on a variety of matters relevant to the exercise of an informed judgment.[2] It must not be misleading in any material respect.[3] And, under Rule X–14A–2 (R. 89–90), the various matters to be acted upon at the meeting pursuant to the proxy must be set forth in ballot form so that the security holders may be afforded an opportunity to vote approval or disapproval of each specific item. The Rule most immediately in-

[1] Rules X–14A–1, X–14A–4 (R. 88, 91).
[2] Schedule 14A (R. 97–112).
[3] Rule X–14A–5 (R. 92).

volved is Rule X–14A–7, which provides in pertinent part:

> In the event that a qualified security holder of the issuer has given the management reasonable notice that such security holder intends to present for action at a meeting of security holders of the issuer a proposal which is a proper subject for action by the security holders, the management shall set forth the proposal and provide means by which security holders can make a specification as provided in rule X–14A–2. Further, if the management opposes such proposal, it shall, upon the request of such security holder, include in its soliciting material the name and address of such security holder and a statement of such security holder setting forth the reasons advanced by him in support of such proposal: *Provided, however,* That a statement of reasons in support of a proposal shall not be longer than 100 words: *And provided further,* That such security holder and not the management shall be responsible for such statement.

Transamerica Corporation, a Delaware corporation, has outstanding approximately 9,935,000 shares of $2 par value capital stock, which are registered with the Commission and listed on the New York Stock Exchange, the Los Angeles Stock Exchange, and the San Francisco Stock Exchange, all of which are national securities ex-

changes (R. 21a). The shares are held by approximately 151,000 shareholders (R. 53a).

John J. Gilbert, a duly qualified stockholder of Transamerica Corporation, early in January 1946, by letter to the management, submitted four proposals which he stated his intention to present for action by shareholders at the next annual stockholders' meeting, to be held on the last Thursday in April 1946. The proposals were as follows (R. 10a–13a):

(1) To have the independent public auditors of the books of the corporation elected by the stockholders.

(2) To amend By-Law 47 so as to eliminate therefrom the requirement that notice of any proposed alteration or amendment of the By-Laws be contained in the notice of meeting. (Gilbert made it clear in his communication to the company (R. 10a–13a) that his purpose was not to prevent actual notice of such matters to the security holders—notice being assured in any event under the Commission's proxy rules. His purpose, as he stated, was to prevent the management from exercising its asserted power to block action on stockholders' proposals by the technical device of excluding such proposals from the notice of meeting.)

(3) To change the place of annual meeting of the corporation from Wilmington, Delaware, to San Francisco, California.

(4) To require that an account of the proceedings of the annual meeting be sent to all stockholders of the corporation.

The directors of Transamerica took the position, in correspondence with the Commission, that these proposals were not proper subjects for action by the security holders within the meaning of the Commission's Rule X–14A–7. The Commission stated that in its view they were proper (R. 26a–42a). Accordingly, when the management, in disregard of the Commission's advice, mailed out its soliciting material without setting forth the proposals in compliance with Rule X–14A–7, the Commission sought injunctive relief in the District Court of the United States for the District of Delaware.[4]

The District Court permitted the meeting to be convened for the transaction of ordinary business but ordered that it thereafter be adjourned pending determination by the court as to whether Gilbert's proposals were proper subjects for action by the security holders (R. 56a–57a). The court subsequently ruled that the proposal dealing with the election of auditors was a proper

[4] Gilbert's proposals were described in the proxy soliciting material under the provisions of Item 18 of Schedule 14A (R. 112). The management did not, however, print the statement not exceeding 100 words which Gilbert had submitted in support of each proposal, and, more important, the management did not afford the security holders an opportunity to vote on the proposals—all in contravention of the provisions of Rule X–14A–7.

subject for action by the security holders, but that the other proposals were not (R. 62a–75a, 79a–80a).[5] The court ordered resolicitation of the security holders on the auditor proposal, but this mandate has been stayed during the pendency of appellate proceedings.

Cross appeals were taken to the Circuit Court of Appeals for the Third Circuit by the Commission and by the petitioners. The Circuit Court of Appeals sustained the Commission's position as to all of Gilbert's proposals, and also sustained the final judgment of the District Court against various technical objections advanced by the Transamerica management. Thus, the position of the Commission was fully upheld on both appeals.

ARGUMENT

As appears from the opinions of the courts below, the principal argument of the petitioners in the previous stages of the case was that a proposed By-Law amendment which is an otherwise proper subject for action by the security holders under State law can be rendered improper by the simple device of excluding it from the notice of meeting. Such exclusion, it was argued, would make it mandatory for the management to rule the proposal "out of order" at the meeting by

[5] Prior to the institution of the District Court proceeding the directors had themselves adopted the third proposal, dealing with the place of meeting, so that issue has been mooted.

virtue of a requirement under State law that proposed By-Law amendments be set forth in the notice of meeting. The consequence, it was said, was that a proposal so excluded could not be deemed to be a "proper subject for action by the security holders" within the meaning of Rule X–14A–7.

The court below rejected this view of the Rule, accepting the Commission's construction that the term "proper subject for action by the security holders" embraced all proposals which are within the compass of stockholder action under State law without reference to procedural devices which might be employed under State law to prevent such action. The court ruled that even if the particular blocking device adopted in the present case were not actually invalid under State law, it could not be employed to render nugatory the overriding federal policy represented by Section 14 (a) of the Securities Exchange Act and Rule X–14A–7 thereunder.

This basic issue appears to have been dropped for purposes of the petition for writs of certiorari, and is mentioned here only for the light that it sheds on many of the minor points that are relied upon. The enumeration in the petition of Questions Involved includes the question "Were Gilbert's proposals 'a proper subject for action' by stockholders within the meaning of Rule X–14A–7?" (Pet. 7). However, this issue

is not adverted to in the discussion of Reasons for Granting the Writs, except that the last proposal, dealing with a report to the stockholders of the proceedings at the annual meeting, is said to be beyond the powers of the stockholders under Delaware law.

While the District Court and the Circuit Court of Appeals took a somewhat different approach to the construction of Rule X–14A–7, they were wholly in accord in overruling a large number of objections which, presumably because the courts thought them insubstantial, are the subject of little or no discussion in the written opinions. It is these secondary objections, or rather a selected few of them which appear to constitute the sole basis for the present petition. They are discussed below *seriatim*. We think that these objections are in fact insubstantial, that the asserted conflicts with decisions of other circuits and of this Court concerning some of the points do not exist, and that, except in the case of the first of the objections, which is an assault upon the validity of Rule X–14A–7, no questions of public interest are presented.

1. It is argued that Rule X–14A–7 is unauthorized by Section 14 (a) of the Act. Section 14 (a), it is noted, does not expressly impose a duty upon a management to solicit proxies upon stockholders' proposals, but provides only that solicitation of proxies (by any person) may not be undertaken "in contravention of such rules and

regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors." It is argued, in effect, that under this standard the only conditions precedent to solicitation which the Commission may impose are conditions designed to ensure "disclosure * * * concerning matters upon which the solicited proxies were to be used * * *" (Pet. 8).

Such a construction is not justified by the language of Section 14 (a) or by its legislative history, and would frustrate fulfillment of the Congressional design embodied in the statute. The ruling of the court below on this issue is correct, and there is no suggestion of conflict of decisions.

The Securities Exchange Act is a many-sided statute which was designed to stabilize the national economy against the shocks produced by a faulty investment system in need of adjustment to modern conditions.[6] Basic to the problem, the Congress believed, was the development of large corporations, the geographical diffusion of their security holders, and the evils that ensued from the divorce of ownership from control.[7] It was

[6] See Statement of Purposes in Section 2 of the Act.

[7] H. Rep. No. 1383, 73d Cong., 2d Sess. (1934), 3, 5. It is interesting to note that all the directors of Transamerica are the beneficial owners of only one-half of one percent of the outstanding securities (R. 15a–16a). This includes 21,500 shares held by a trust managed by L. M. Giannini (R. 16a).

thought that investor confidence could not be restored until corporate trustees more adequately represented their *cestuis* and were rendered amenable to internal controls.[8] Accordingly, among other remedies, Congress adopted Section 14 (a) in an attempt to restore "fair corporate suffrage" by employing the federal power to curb abuses of the proxy machinery by which entrenched minorities had denied to security holders any effective voice in the management of their corporations.[9]

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[8] H. Rep. No. 1383, 73d Cong., 2d Sess. (1934) 5.

[9] The problem was put as follows by the House Committee on Interstate and Foreign Commerce (H. Rep. No. 1383, 73d Cong., 2d Sess. (1934) 13–14): "Fair corporate suffrage is an important right that should attach to every equity security bought on a public exchange. Managements of properties owned by the investing public should not be permitted to perpetuate themselves by the misuse of corporate proxies. Insiders having little or no substantial interest in the properties they manage have often retained their control without an adequate disclosure of their interest and without an adequate explanation of the management policies they intend to pursue. Insiders have at times solicited proxies without fairly informing the stockholders of the purposes for which the proxies are to be used and have used such proxies to take from the stockholders for their own selfish advantage valuable property rights. Inasmuch as only the exchanges make it possible for securities to be widely distributed among the investing public, it follows as a corollary that the use of the exchanges should involve a corresponding duty of according to shareholders fair suffrage. For this reason the proposed bill gives the Federal Trade Commission power to control the conditions under which proxies may be solicited with a view to preventing the recurrence of abuses which have frustrated the free exercise of the voting rights of stockholders."

So far as is relevant here, the position of the Commission, in brief, is that if the Congressional design is to be made effective the security holders should be informed not only concerning the items the management will vote *for,* but also the items (presented by minority groups) that the management will vote *against;* and, further, that the security holders should be afforded an opportunity to instruct the persons soliciting their proxies as to their wishes on each specific matter to be proposed at the meeting. Only in this manner can the proxy machinery perform the function of providing a reasonable substitute for the earlier "town-meeting" form of corporate meeting which has been rendered impossible by modern conditions of corporate growth and the wide distribution of corporate securities. Nevertheless, the Transamerica management objects to being instructed by the solicited security holders as to how to vote except on items of business which it, the management proposes, even where it knows, on the basis of formal notice, that other proposals will be tendered by stockholders for consideration at the meeting.

There has been no showing that such an extraordinary gap in the protective scheme is envisioned in the language of the statute or in its legislative history. Under the circumstances it seems to us that to state the argument is to refute it.

2. Petitioners argue that because they have been found to have violated Rule X–14A–7 only as to Gilbert's proposals, paragraph (3) of the District Court's order (affirmed by the Circuit Court of Appeals), enjoining the petitioners from soliciting proxies "without complying fully with Section 14 (a) of the Securities Exchange Act of 1934 and Proxy Rules X–14A–7 and X–14A–2 thereunder" (R. 82a), is too broad. The "sweep of the injunction" is said to be in conflict with the principles enunciated in *National Labor Relations Board* v. *Express Publishing Co.*, 312 U. S. 426, and *May Department Stores Co.* v. *National Labor Relations Board*, 326 U. S. 376. These cases state the familiar rule that a court or agency may not as a matter of course "enjoin violations of all the provisions of the statute merely because the violation of one has been found."[10] On the other hand, these cases also recognize that—

> A federal court has broad power to restrain acts which are of the same type or class as unlawful acts which the court has found to have been committed or whose commission in the future, unless enjoined, may fairly be anticipated from the defendant's conduct in the past. * * *
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> To justify an order restraining other violations it must appear that they bear some

[10] *National Labor Relations Board* v. *Express Publishing Co.*, 312 U. S. at 437.

> resemblance to that which the employer has committed or that danger of their commission in the future is to be anticipated from the course of his conduct in the past.[11]

Since most of the points on which petitioners relied below have been abandoned, the full scope of their resistance to the proxy rules is not apparent from the present petition. As appears from the opinions below, petitioners claimed, among other things, an unfettered discretion to keep *all* stockholder proposals from being acted upon at the annual meeting by the dubious device of excluding them from the notice of meeting. They argued that the proxy rules actually permitted them to do so, and that, if the rules did not, they were invalid. The scope of the injunction was no broader than the claim of the right to violate the rules.

3. It is said that the court below did not take account of changed circumstances, and it is asserted vaguely that its failure to do so is in conflict with decisions of this Court to the effect that an appellate tribunal should take account of changed circumstances (Pet. 13–15). This point was never urged on the court below, and is in any event without substance.

As previously noted, Gilbert's proposals were advanced in connection with the 1946 meeting, which the District Court ordered adjourned (after the transaction of ordinary business) pending de-

[11] *Id.*, 435, 437.

termination of the questions raised by the litigation. The District Court then ordered resolicitation on the auditor proposal, but stayed its mandate during the pendency of the appellate proceedings. The appeals were argued before the Circuit Court of Appeals several months prior to the 1947 meeting, and the imminence of the 1947 meeting was directed to the attention of that Court. The Circuit Court of Appeals did not render its decision until after the 1947 meeting, and then its decision in effect was that there should be resolicitation as to all of Gilbert's proposals. The fact that the 1947 meeting has intervened is the change of circumstances alluded to.

It is not claimed, nor could it be, that the holding of the 1947 meeting has rendered the controversy moot.[12] It is claimed only that some technical difficulties will be presented by reason of the fact that the 1947 meeting has already been held and that the body of stockholders is no longer the same as in 1946 (Pet. 15). The resolution of such difficulties, if they exist, can certainly be undertaken by the District Court, subject to the supervision of the Circuit Court of Appeals. Since those courts have not even been asked to resolve these problems there is no warrant for

[12] See *Southern Pacific Terminal Co.* v. *Interstate Commerce Commission*, 219 U. S. 498, 514–16; *McGrain* v. *Daugherty*, 273 U. S. 135, 180–82; *Boise City Irr. & Land Co.* v. *Clark*, 131 Fed. 415, 418–19 (C. C. A. 9).

now urging consideration of the problem by this Court.

4. It is said that the effect of the decision below is to repose in the Commission the power to dictate the terms of a notice of meeting even though proxy rules do not expressly specify what the notice must contain nor require it to be filed prior to solicitation (Pet. 9).

At the heart of the rules, of course, is the requirement of notice as to what will be done at the meeting. The Commission cannot undertake to anticipate, and to proscribe in its rules, every procedural device that may be employed to block stockholder action; in any race to find and plug loopholes the Commission would invariably lag behind the corporate bar. The proxy rules would be meaningless if affirmative rights granted by them to stockholders could be frustrated through procedural devices not expressly forbidden by the rules. Where such procedural devices are resorted to, the district courts, upon application by the Commission, and in the exercise of their equity jurisdiction, can make any decree reasonably necessary to effectuate the statutory rights under attack. That is all that happened here, and it is all that the complaint above described is directed to.

At most, the issue is one as to appropriateness of the particular remedy granted. The issue is not one of general importance and no conflict of decisions is claimed.

5. Even more insubstantial is the complaint that an amended notice of meeting was ordered to be sent to stockholders from whom no proxies had been solicited—namely, the 1,300 foreign stockholders out of Transamerica's total of 151,000 stockholders (Pet. 8). Transamerica does not object to the mailing of the notice of meeting to all stockholders of record, domestic or foreign. Indeed, its point is that this is a prerequisite under State law, to the holding of a valid meeting. We submit that once it be established that the Commission was warranted in insisting, for the purposes of controlling Transamerica's solicitation of proxies from domestic security holders, upon a notice of meeting broad enough to include Gilbert's proposals, it is immaterial that compliance with this requirement incidentally affects the scope of the notice of meeting sent also to foreign security holders.[13]

To make the statutory rights involved fully effective, the District Court had no alternative but to order an amended notice of meeting to be sent to all the stockholders of Transamerica.

6. For the reasons stated above, that portion of the decree relating to the notice of meeting, like

[13] If there were any merit in this argument of Transamerica it would be possible for its management by arbitrarily deciding to refrain from soliciting a single security holder, domestic or foreign, to argue that this precludes any control over the content of the proxy material sent to the remaining security holders solicited by the management.

the decree as a whole, was an exercise of the District Court's jurisdiction, as set forth in Section 27 of the Act, "to enforce any liability or duty created by this title or the rules and regulations thereunder;" it was not, as petitioners mistakenly claim, the enforcement of a State-created right (Pet. 9–10). It is true that the Commission expressed the view in its early correspondence with the management that the use of the notice of meeting as a device for blocking stockholder action was in violation of Delaware law (R. 32a-33a). However, neither the Commission nor the court below relied upon that proposition, for the federal policy embodied in Section 14 (a) and the proxy rules issued thereunder was obviously paramount.

7. Only one of Gilbert's proposals—the "straight resolution" requiring the directors to send to the stockholders a summary of the proceedings at the annual meeting—is now claimed to be beyond the powers of the security holders under State law (Pet. 10). Because an expenditure of corporate funds is necessarily involved,[14] and because under Delaware law and the company's charter and bylaws "the management of Transamerica is vested in its directors" (Pet. 10), it is said that the matter is one within the exclusive domain of the directors. No authority is advanced in support of this novel position. The

[14] The management estimated the annual cost to be some $20,000.

proposal appears to be clearly within the general rule permitting stockholders to act upon matters concerning the internal government of the corporation, as distinct from the actual conduct of the corporate business.[15] At the most there is involved a narrow question of State law.

8. We have discussed all the points raised in the discussion of Reasons for Granting the Writs. We assume that the various additional arguments implicit in petitioners' Statement of the Case (Pet. 2–7) are not relied upon for purposes of the petition. They go to the contention that the requirements of Rule X–14A–7 are in effect optional with the management and that the petitioners therefore did not really violate the Rule. Although these arguments were vigorously pressed below, neither of the courts below deemed them sufficiently substantial to warrant discussion.

CONCLUSION

For the reasons stated, the petition for writs of certiorari should be denied.

Respectfully submitted.

PHILIP B. PERLMAN,
Solicitor General.

ROGER S. FOSTER,
Solicitor,
Securities and Exchange Commission.

DECEMBER 1947.

[15] See *5 Fletcher on Corporations* (1931 Ed.) § 2097; 8 Id. §§ 4166–67, 4170–72, 4177–78.

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